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PAGE 01 OECD P 06763 01 OF 04 182007Z

73

ACTION EUR-25

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PAGE 02 OECD P 06763 01 OF 04 182007Z

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DEPT PASS TREAS FOR BLAKE, COMMERCE FOR NEUMANN

E.O. 11652: N/A

TAGS: EFIN, OECD

SUBJECT: INVISIBLES COMMITTEE SPECIAL MEETING ON DIRECT
INVESTMENT

REF: (A) DAF/INV/74.1

(B) STATE 030543

(C) WORKING PAPER NO. 1 (IC-MARCH 1, 1974)

1. SUMMARY: INVISIBLES COMMITTEE (IC) HELD ANNUAL REVIEW OF INWARD DIRECT INVESTMENT (DI) MARCH 12, 1974. SEVERAL GENERAL QUESTIONS WERE RAISED INCLUDING: (A) RIGHT OF POLITICAL SUBDIVISIONS TO RAISE RESTRICTIONS AFTER HOST COUNTRY HAS JOINED CAPITAL MOVEMENTS CODE (CMC), (B) PREFERENTIAL TREATMENT FOR DI IN PRODUCTIVE VERSUS SERVICE INDUSTRIES, (C) EXTENT TO WHICH NEGOTIATED TRADE RELATIONSHIPS BETWEEN TWO COUNTRIES SHOULD BE ALLOWED TO HAMPER DI FLOWS INTO ONE OF THOSE COUNTRIES, (D) EXTENT TO WHICH SECTORAL ECONOMIC QUESTIONS (PENETRATION OF DOMESTIC INDUSTRIAL SECTORS, IMPACT OF SECTOR ON HOST'S BALANCE OF PAYMENTS) SHOULD LIKEWISE BE ALLOWED TO DETERMINE ACCEPTABILITY OF SPECIFIC DI TRANSACTIONS, (E) POSSIBLE TRADE DISTORTING EFFECTS OF RESTRICTIONS AGAINST LOCAL BORROWING BY FOREIGN-OWNED FIRMS; (F) EFFORTS OF A NUMBER OF COUNTRIES (GERMANY, U.S., FRANCE) TO IMPROVE DI STATISTICS. NO DECISION MADE ON NEXT ANNUAL MEETING THIS SUBJECT. END SUMMARY.

2. GENERAL COMMENTS: IC FOCUSED PRIMARILY ON COUNTRY-BY-COUNTRY DISCUSSION OF INVESTMENT CASES RAISED REF C. EXPERTS FROM NATIONAL CAPITALS SEEMED WELL PREPARED ANSWER QUESTIONS CIRCULATED IN ADVANCE. HOWEVER, SOME WERE UNWILLING TO GO VERY EXTENSIVELY INTO DETAILS OF SPECIFIC CASES DUE TO CONFIDENTIAL NATURE. CONCLUSIONS
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PAGE 03 OECD P 06763 01 OF 04 182007Z

TO BE DRAWN FROM SESSION WILL BE SUBJECT OF SUBSEQUENT REGULAR SESSION IC.

3. NUMBER OF GENERAL QUESTIONS AROSE DURING DISCUSSIONS OF CERTAIN CASES:

(A) RIGHT OF POLITICAL SUBDIVISIONS TO RAISE RESTRICTIONS AFTER HOST COUNTRY HAD JOINED CMC WAS SUGGESTED AS POSSIBLE SUBJECT FOR FUTURE DELIBERATIONS

BY IC. U.S. CASE SEEMED ADEQUATELY COVERED BY RESERVATION CONCERNING EXCLUSION FROM CODE OF MATTERS COMING WITHIN PURVIEW OF STATE REGULATORY POWERS. GENERAL SITUATION VIS-A-VIS COUNTRIES NOT HAVING THIS TYPE RESERVATION REMAINS UNCLEAR.

(B) THROUGHOUT DISCUSSION, AND ESPECIALLY IN CASES OF AUSTRIA, ITALY, AUSTRALIA, SWEDEN, SPAIN, FRANCE, IT WAS APPARENT THAT CONTROL AUTHORITIES TYPICALLY GIVE STRONG PREFERENTIAL TREATMENT TO INVESTMENTS IN PRODUCTIVE SECTOR (I.E., OUTPUT OF REAL GOODS) AS COMPARED TO INVESTMENTS IN SERVICE SECTOR. U.S. REP POINTED OUT NO BASIS FOR THIS DISTINCTION EXISTS IN CMC.

(C) IN ITALIAN AND SPANISH CASES, QUESTIONS WERE RAISED REGARDING EXTENT TO WHICH NEGOTIATED TRADE AGREEMENTS BETWEEN TWO COUNTRIES MIGHT HAMPER DI FLOWS INTO ONE OF THOSE COUNTRIES. FOR EXAMPLE, IF DI PROJECT WERE TO RESULT IN INCREASED LOCAL PRODUCTION OF IMPORTED ITEMS COVERED BY TRADE AGREEMENTS WITH THIRD COUNTRIES, CONTROL AUTHORITIES MIGHT REJECT DI PROJECT IN EFFORT TO MAINTAIN EXISTING TRADE RELATIONSHIPS. THIS KIND OF

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PAGE 01 OECD P 06763 02 OF 04 182012Z

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PAGE 02 OECD P 06763 02 OF 04 182012Z

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DISCRIMINATORY TREATMENT WOULD APPEAR TO HAVE NO BASIS
UNDER CMC.

(D) IN SPANISH CASE, SECTORAL ECONOMIC QUESTIONS
APPEARED TO BE GIVEN SPECIAL WEIGHT BY CONTROL AUTHORI-
TIES. HEAVY PENETRATION OF AN IMPORTANT DOMESTIC SECTOR,
ESPECIALLY WHEN THAT SECTOR IS MAJOR FOREIGN EXCHANGE
EARNER, MIGHT LEAD TO LESS FAVORABLE TREATMENT FOR
FURTHER DI IN THAT SECTOR.

(E) IN RESPONSE TO U.S. QUESTION CONCERNING DOMESTIC
BORROWING BY DIRECT INVESTORS IN U.K., U.K. REP
ACKNOWLEDGED THAT SUCH BORROWING MIGHT BE APPROVED IF IT
COULD BE SHOWN TO HAVE NET FAVORABLE IMPACT ON DOMESTIC
SITUATION OR INTERNATIONAL PAYMENTS POSITION. U.K.
AUTHORITIES CONSIDERED IT APPROPRIATE FOR DIRECT
INVESTORS TO BRING IN NEW FUNDS, SINCE INVESTMENT
ACTIVITY WOULD SUBSEQUENTLY LEAD TO VARIOUS DEMANDS FOR
FOREIGN EXCHANGE (E.G., IMPORTS OR REPATRIATION OF
PROFITS). IN SITUATIONS WHERE INVESTMENT WAS EXPECTED TO
GENERATE SUBSTANTIAL FOREIGN EXCHANGE EARNINGS, GREATER
ACCESS TO LOCAL FINANCING MIGHT BE GRANTED. U.S. REP
SUGGESTED THIS MIGHT HAVE DISTORTING EFFECT ON TRADE,

SINCE DIRECT INVESTORS WOULD BE ENCOURAGED TO SLANT PRODUCTION TOWARD EXPORT MARKET IN ORDER TO ACHIEVE ACCESS TO DOMESTIC CHANNELS OF FINANCING. (SEE ALSO PARA 4(C) BELOW.)

(F) NUMBER OF EXPERTS REPORTED THEIR GOVERNMENTS WERE MAKING MAJOR EFFORT TO IMPROVE DI STATISTICS (INCLUDING FRANCE, GERMANY, U.S.). IC AGREED THAT NO BAR EXISTS IN CMC TO EXPANSION OF DATA-COLLECTING ACTIVITIES.

4. U.S. QUESTIONS OF FOREIGN EXPERTS: U.S. REP (TANNER) EXAMINED AUSTRALIAN, AUSTRIAN, FRENCH AND U.K. DELEGATIONS FURTHER AS REQUESTED REF B. COMMITTEE UNABLE TO DISCUSS TURKEY DUE TO LACK OF TIME.

(A) AUSTRALIAN REP NOTED THAT IF PROPOSED TAKEOVER IS IN "NATIONAL INTEREST" AND CONTRIBUTES TO COUNTRY'S LIMITED OFFICIAL USE

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PAGE 03 OECD P 06763 02 OF 04 182012Z

ECONOMIC AND INDUSTRIAL NEEDS, APPLICATION USUALLY APPROVED. SIZE OF PROPOSED INVESTMENT AS WELL AS SIZE OF INVESTOR NOT FACTOR IN GRANTING APPROVAL. FOREIGN INVESTMENTS ARE FAVORED IN MANUFACTURING AND TOURISM, BUT TEND TO BE DISCOURAGED IN EXPLOITATION OF MINERAL RESOURCES AND IN INSURANCE. PRESENT TAKEOVER LEGISLATION (COVERING MAINLY PURCHASE OF SHARES) IS SCHEDULED TO LAPSE END 1974 AND WILL BE REPLACED BY MORE COMPREHENSIVE LEGISLATION THAT WILL BETTER DEFINE "NATIONAL INTEREST." U.S. REP ASKED THAT AUSTRALIAN AUTHORITIES CONSIDER WAYS OF COMPLYING WITH AIM OF CMC TO MAXIMUM EXTENT POSSIBLE IN DRAFTING NEW LEGISLATION. AUSTRALIAN REP ASSURED IC HIS AUTHORITIES WILL BE INFORMED, AND NOTED THAT INTEREST OF IC THIS MATTER WILL UNDOUBTEDLY HAVE USEFUL IMPACT ON DEVELOPMENT OF AUSTRALIAN POLICY.

(B) AUSTRIA: IT WAS NOTED THAT REGULATIONS ON REAL ESTATE ACQUISITION AND LAND USE ARE DOMAIN OF PROVINCIAL AUTHORITIES AND VARY AMONG PROVINCES. CONSTRUCTION PERMITS FOR HOTELS ARE ISSUED ON BASIS OF LAND USE PLANS, PROTECTION OF ENVIRONMENT (NO SKYSCRAPERS IN RURAL AREAS), AND ADEQUACY OF EXISTING HOTELS, REGARDLESS OF WHETHER DOMESTIC OR FOREIGN OWNED. UPPER TYROL ONLY PROVINCE REFUSING LAND SALE TO FOREIGNERS. ELSEWHERE, PURCHASE OF PERSONAL RESIDENCE IS PERMITTED ONLY FOR FULL-TIME OCCUPANCY, EXCEPT IN SPECIAL CASES. NO CONCLUSION DRAWN ON QUESTION OF EXTENT TO WHICH LAND PURCHASE SHOULD BE COVERED BY ITEM I OR VI OF LIST A.

(C) U.K. REP NOTED THAT LOCAL FINANCING IS AVAILABLE TO DIRECT INVESTORS FROM OUTSIDE EC FOR NEW INVESTMENTS IN "ASSISTED" AREAS (SEE ALSO PARA 3(E) ABOVE). OTHERWISE, AVAILABILITY OF LOCAL FUNDS FOR INVESTMENT DEPENDS ON IMPORTANCE OF PROJECT TO U.K. ECONOMY. IF EXPECTED TO RESULT IN ADDITIONAL EXPORTS OR IMPORT SUBSTITUTION,

WORKING CAPITAL PLUS PORTIONS OF FIXED CAPITAL MAY BE
RAISED LOCALLY. LOCAL BORROWING IS NOT PERMITTED FOR
REAL ESTATE AND FINANCIAL INVESTMENTS.

(D) FRANCE: GENERALLY, DI IS ASSUMED TO EXIST
WHENEVER AGGREGATE TOTAL OF FOREIGN OWNERSHIP IN LISTED
FRENCH FIRM EXCEEDS 20 PERCENT OF OUTSTANDING SHARES,
WHETHER SUCH SHARES ARE HELD BY ONE OR MANY FOREIGNERS,
AND WHETHER OR NOT FOREIGN INVESTORS (IF MORE THAN ONE)
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PAGE 04 OECD P 06763 02 OF 04 182012Z

ARE RELATED. HOWEVER, IN CERTAIN CASES, LESS THAN
20 PERCENT FOREIGN OWNERSHIP MAY BE CONSIDERED TO BE DI
IF NATURE OF DOMESTIC AND FOREIGN HOLDINGS IS SUCH THAT
FOREIGN INTERESTS COULD CONTROL, OR IF FIRM INVOLVED IS
OF SPECIAL IMPORTANCE TO FRENCH ECONOMY. DECISIONS THEN
MADE ON CASE-BY-CASE BASIS.

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PAGE 01 OECD P 06763 03 OF 04 182021Z

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PAGE 02 OECD P 06763 03 OF 04 182021Z

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LIMITED OFFICIAL USE SECTION 03 OF 04 USMISSION OECD PARIS 06763

5. FOREIGN QUESTIONS OF U.S. EXPERTS: IN RESPONSE TO
GENERAL QUESTIONS PG 17 REF C, U.S. EXPERT (NEUMANN)
REPORTED ON CURRENT U.S. FOREIGN DI POLICY AND
CONGRESSIONAL REACTION TO RECENT INCREASE IN FOREIGN
INVESTMENT IN U.S. DUE TO LACK OF TIME, APPLICATION OF
ANTITRUST LAWS WAS DISCUSSED ONLY BRIEFLY AND VERY FEW
QUESTIONS WERE RAISED REGARDING INDIVIDUAL INVESTMENT
PROJECTS PRESENTLY IN LITIGATION:

(A) CONCERNING FOREIGN INVESTMENT POLICY, U.S.
EXPERT REFERRED TO FEB 1974 HOUSE FOREIGN AFFAIRS
COMMITTEE HEARING WHEREIN FLANIGAN OUTLINED U.S. OPEN-
DOOR POLICY FOR PROSPECTIVE FOREIGN INVESTORS AND
REAFFIRMED POLICY OF NATIONAL TREATMENT FOR FOREIGN FIRMS
OPERATING IN U.S. IT WAS EMPHASIZED THAT USG OFFERS NO
SPECIAL INCENTIVES TO ATTRACT FOREIGN INVESTORS AND
IMPOSES NO SPECIAL BARRIERS EXCEPT AS NOTED IN U.S.
RESERVATION ON DI ITEM. U.S. POLICY PREFERENCE FOR
RELIANCE ON MARKET FORCES IN WORLD ECONOMY AND MINIMIZA-
TION OF RESTRICTIONS IS CONSISTENT WITH LIBERAL U.S.
POSITION UNDER CMC AND IS ALSO REFLECTED IN OUR BILATERAL

TREATIES. U.S. ADMINISTRATION CONTEMPLATES NO CHANGES IN THIS POLICY AT THIS TIME.

(B) CONCERNING CONGRESSIONAL RESPONSE TO INCREASING PUBLIC SENSITIVITY TO EXPANSION OF CERTAIN TYPES OF FOREIGN INVESTMENTS IN U.S. (E.G., REAL ESTATE IN URBAN, RESORT, AND AGRICULTURAL AREAS), U.S. EXPERT STRESSED THAT PROPOSALS FOR LEGISLATION REFLECT PRIMARILY CONCERNS OF CERTAIN CONGRESSMEN ABOUT CASES WITHIN THEIR DISTRICTS, AND DO NOT REPRESENT SHIFT IN NATIONAL POLICY. WITHOUT DESCRIBING DETAILS OF VARIOUS EXISTING AND PROPOSED BILLS, EXPERT ASSURED IC THAT U.S. ADMINISTRATION WOULD NOT SUPPORT RESTRICTIVE LEGISLATION. THOUGH OUTCOME OF CONGRESSIONAL HEARINGS IS ADMITTEDLY UNCERTAIN AT THIS TIME, ALL BILLS STILL PENDING WILL AUTOMATICALLY DIE AT END OF CURRENT CONGRESSIONAL SESSION, AND WOULD LIMITED OFFICIAL USE

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PAGE 03 OECD P 06763 03 OF 04 182021Z

HAVE TO BE REINTRODUCED NEXT SESSION IF MATTER IS TO BE PURSUED FURTHER.

(C) U.S. EXPERT NOTED THAT ADMINISTRATION SUPPORTS BILL PROPOSING COMPREHENSIVE PROGRAM OF DATA-GATHERING AND ANALYSIS TO DETERMINE IMPACT OF FOREIGN INVESTMENT IN U.S. CONFIRMED THAT NEW BENCHMARK SURVEY ON INWARD DIRECT AND PORTFOLIO INVESTMENT IS NEEDED TO UPDATE MOST RECENT SURVEYS (1959 FOR FOREIGN DIRECT INVESTMENT, 1949 FOR PORTFOLIO INVESTMENT IN U.S.) AND EXPAND COVERAGE. RESPONDING TO COMMENT THAT A NUMBER OF OTHER COUNTRIES PLACE CONSIDERABLE RELIANCE ON U.S. STATISTICS FOR INVESTMENTS IN AND BY THEIR OWN COUNTRIES, U.S. EXPERT STATED THAT HIGH-PRIORITY BENCHMARK SURVEY OF FOREIGN DI ABROAD IS IN INITIAL STAGE; WHILE FUNDING AND RESOURCES FOR BENCHMARKS ON INWARD INVESTMENT NOT YET PROVIDED.

(D) U.S. REP NOTED THAT LEGAL AND ANTITRUST DEFENSES AGAINST TAKEOVER ARE SAME WHETHER FOREIGN OR DOMESTIC PURCHASER IS INVOLVED, AND THAT ANTITRUST LAWS SHOULD NOT BE CONSIDERED TO HANDICAP FOREIGN TAKEOVERS WHERE IT IS CLEAR THAT COMPETITION WILL NOT BE REDUCED.

6. U.S. STATEMENT ON GENERAL POLICY TOWARD DI IN FINANCIAL SECTOR (REF C, PG 18-19): U.S. EXPERT (BLAKE) NOTED THAT MAIN REASON FOR CURRENT INTEREST IN FOREIGN BANKING FACILITIES IN U.S. IS THEIR RAPID EXPANSION. PRESENTLY THERE ARE OVER 60 FOREIGN BANKS OPERATING IN U.S., OF WHICH GREAT MAJORITY WERE ESTABLISHED IN PAST SEVERAL YEARS. ALTHOUGH DI IN U.S. BANKING FACILITIES IS LESS THAN \$1 BILLION, MORE ACCURATE INDICATOR OF SIZE AND SIGNIFICANCE OF FOREIGN BANKING PRESENCE WOULD BE SIZE OF BANKING ASSETS. FOREIGN BANKS IN U.S. HAVE ASSETS OF \$35 BILLION COMPARED WITH \$762 MILLION FOR TOTAL INSURED U.S. BANKS.

7. U.S. EXPERT DESCRIBED REGULATIONS GOVERNING DUAL
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PAGE 01 OECD P 06763 04 OF 04 182026Z

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PAGE 02 OECD P 06763 04 OF 04 182026Z

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RELATED BILLS HAVE BEEN INTRODUCED IN CONGRESS BY REPS PATMAN AND REES, HEARINGS HAVE NOT BEEN HELD AND, DUE TO TIME RESTRAINT, IT IS DOUBTFUL ANY NEW LEGISLATION THIS SUBJECT WILL BE APPROVED BY CONGRESS DURING 1974. U.S. ADMINISTRATION EXPECTED TO OPPOSE PATMAN BILL WHEN HEARINGS ARE HELD.

8. U.S. EXPERT (BLAKE) PROVIDED COMMITTEE WITH ESSENTIAL BACKGROUND ON FOUR CASES OF FOREIGN INVESTMENT IN U.S. BANKING INDUSTRY RAISED REF C AFTER NOTING THAT PERJURATIVE TONE OF REF C WAS IN HIS VIEW INAPPROPRIATE SINCE MOST OF CASES MENTIONED HAD BEEN APPROVED BY BANK AUTHORITIES CONCERNED. CASES WERE: (A) SINDONA PURCHASE OF EQUITY IN FRANKLIN N.Y. CORP, (B) SAFRA PURCHASE OF EQUITY IN KINGS LAFAYETTE CORP., (C) BARCLAYS BANK EFFORT TO ACQUIRE LONG ISLAND TRUST, AND (D) LLOYDS BANK PURCHASE OF FIRST WESTERN BANK AND TRUST. U.S. EXPERT NOTED THAT ONLY CASE (C) WAS BARRED BY AUTHORITIES. FIRST TWO CASES INVOLVED PURCHASES OF BANK INTEREST BY FOREIGN INDIVIDUALS; STATE REGULATORY AUTHORITIES WERE INVOLVED ONLY TO ASSURE NO DIMINUATION OF COMPETITION RESULTED. THIRD CASE WAS DISAPPROVED BY STATE BANKING AUTHORITY SINCE IT WOULD HAVE REDUCED COMPETITION. HOWEVER, BARCLAY'S WAS LATER GRANTED AUTHORITY TO PURCHASE A DIFFERENT N.Y. BANK WHERE IT WAS SHOWN THAT PURCHASE WOULD NOT DIMINISH COMPETITION. U.S. EXPERT POINTED OUT THAT IN CASE (D), FOREIGN PURCHASER WAS ACTUALLY IN PREFERRED POSITION AS COMPARED WITH POTENTIAL DOMESTIC PURCHASER, SINCE PURCHASE BY AN EXISTING STATE BANK OF EQUIVALENT SIZE WOULD HAVE REDUCED COMPETITION. QUOTING FROM U.S. DEP. ASST. ATTORNEY-GENERAL BAKER, EXPERT NOTED THAT U.S. ANTITRUST ENFORCEMENT PROGRAM HAS THUS CREATED -- AND MAY IN FUTURE CREATE MORE -- OPPORTUNITIES FOR ENTRY INTO U.S. MARKETS BY INTERNATIONAL BANKS. BROWN

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Disposition Date: 28 MAY 2004
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